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No. 88-1520

IN THE

Supreme Court of the United States

OCTOBER TERM, 1988

MEDICAL MALPRACTICE INSURANCE ASSOCIATION,

Petitioner,

v.

SUPERINTENDENT OF INSURANCE OF THE STATE OF NEW YORK,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

REPLY BRIEF FOR PETITIONER

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ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

REPLY BRIEF FOR PETITIONER

The petitioner, Medical Malpractice Insurance Association ("MMIA"), respectfully submits this reply brief to Respondent's Brief in Opposition to Petition for Writ of Certiorari.

I.

The Holding of the Court Below That An Insurer May Be Compelled to Operate at a Loss Requires Immediate Review by This Court

The New York Court of Appeals now has made clear that this case involves a novel interpretation of federal constitutional law, which requires immediate review by this Court. In *Medical Malpractice Insurance Association v. Cuomo*, No. 88, slip op.

(N.Y. May 2, 1989), the New York Court of Appeals rejected MMIA's constitutional challenge to a retroactive taking of funds held by MMIA. In a memorandum opinion, a copy of which is annexed as Appendix A to this reply brief, the court stated as follows:

> We have recently determined that the Legislature may require the Medical Malpractice Insurance Association (MMIA) to operate at a loss on a temporary or even continual basis in order to promote affordable medical malpractice coverage.

(App. A at 2a)[1] (citation omitted).[2]

Thus, the issue squarely presented to this Court is whether, as the court below has held, a state can compel an insurer, which is privately funded and controlled, to operate at a loss—even on a "continual basis"—for the benefit of a particular group of policyholders within the state. All other reported decisions upholding state-created joint underwriting associations ("JUA's"), such as MMIA, uniformly have required that the rates charged by the JUA be adequate, reasonable and not confiscatory (*see* MMIA's Petition for a Writ of Certiorari to the Court of Appeals of the State of New York ("Petition") at 16-17, 21).

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1 Parenthetical references to "App." are to the Appendix to this reply brief or to the Petition where indicated. Parenthetical references to "A." are to the Appendix of the Superintendent in the proceedings below. Parenthetical references to "RA." are to the Appendix by MMIA in the proceedings below.

2 In *Cuomo*, a New York law retroactively required MMIA to refund over $10 million which it had lawfully collected and applied to its deficit. The Court of Appeals reversed two lower court decisions sustaining MMIA's assertion of an unconstitutional taking against a motion to dismiss by the State, holding as follows:

> As a creature of statute, MMIA had no vested property interest in those charges and it was within the Legislature's prerogative to direct a refund in an effort to reduce overall health care costs.

(App. A at 2). Consequently, MMIA's $85 million deficit as of December 31, 1985, which is cited in MMIA's Petition for a Writ of Certiorari, at page 4, is now retroactively increased by an additional $10 million.

The New York Court of Appeals alone has erroneously departed from this Court's long-established and consistent teaching that the fifth and fourteenth amendments forbid confiscatory state-prescribed rates (*see* Petition at 13-19).

The Superintendent's contention that the issue is not ripe for review by this Court is ludicrous. Since July 1, 1985, he has set grossly inadequate rates for MMIA's operation. The rates do not enable MMIA to pay its normal operating expenses, including the setting aside of reserves for losses and loss adjustment expenses that will arise under the policies that it is mandated to issue. The risk of professional liability losses and expenses is being shifted from physicians to MMIA upon payment of only a fraction of the costs of such losses and expenses. MMIA is presently forced to assume contractually the full burdens of physicians' loss and expense obligations upon the fiction that the resulting deficits will be recouped from future generations of policyholders. As the court below recognized, even if the recoupment scheme were to work, the calculations of the Superintendent's own actuary showed that MMIA's deficit caused by the 1985-1988 rates cannot be cured until at least the year 2000. *Medical Malpractice Ins. Ass'n v. Superintendent of Ins.*, 72 N.Y.2d 753, 765 (1988) ("*MMIA v. Superintendent*") (Petition, App. A at 10a).

The uncontroverted evidence in the record establishes that MMIA has incurred, and continues to incur, whopping deficits under the rates upheld by the New York Court of Appeals. Under the Superintendent's theory, MMIA would be without constitutional recourse until even larger deficits have accrued and it has become clear, some years in the future, that the deficits cannot be recouped (*see* Respondent's Brief at 8-12).[3]

This Court appropriately has rejected similar ripeness contentions. In *Blanchette v. Connecticut General Ins. Corps.*, 419

3 By the time it is clear that the surcharges cannot recoup the deficits, the Superintendent likely will have become MMIA's liquidator. It is doubtful that he then will bring an action against himself for having failed to set adequate rates, as suggested at page 11 of Respondent's Brief.

U.S. 102 (1974). Justice Brennan, writing for the majority, cogently stated as follows:

> Where the inevitability of the operation of a statute against certain individuals is patent, it is irrelevant to the existence of a justiciable controversy that there will be a time delay before the disputed provisions will come into effect. "One does not have to await the consummation of threatened injury to obtain preventive relief. If the injury is certainly impending that is enough."

Id. at 143 (*quoting Pennsylvania v. West Virginia*, 262 U.S. 553, 593 (1923)) (citations omitted).

Pennell v. City of San Jose, 108 S. Ct. 849 (1988) does not support the Superintendent's ripeness argument in the present case (Respondent's Brief at 10). In *Pennell*, this Court rejected a taking claim as premature because there was no evidence in the record that the statutory provision under challenge had even been relied on by the agency in making its determination.

The Superintendent's assertion that he has never conceded that the rates are inadequate (Respondent's Brief at 9) is belied by Section I of the opinion of the court below, which the Superintendent has adopted as his statement of the case (*id.* at 3). Section I of the opinion states, in pertinent part, as follows:

> Both parties agree that without this consideration of future surcharges, both the primary and the two excess layers of insurance are entirely inadequate to meet the statutory standards of solvency under the Insurance Law (*see*, Insurance Law §§ 5505, 2303).

MMIA v. Superintendent, 72 N.Y.2d 753, 759; (Petition, App. A at 5a).

The Superintendent erroneously asserts that the annual deficits arising from the post-July 1, 1985 inadequate rates have not yet been actuarially projected (Respondent's Brief at 9, 12). In fact, the uncontroverted testimony of the actuaries at the hearing established that the total deficits of the two major New York medical malpractice insurers for the three policy years

1985 through 1988 would be at least $1.6 billion (A. 1197-98, 1221-22, 1283, 1287; *see also* A. 314, 961). The Superintendent's actuary testified that the total deficits arising from the primary rates alone likely would be at least $1.386 billion based on the "scenario" calculations that he had performed for the Superintendent (A. 1197-98, 1221-22). The undisputed testimony of MMIA's actuary shows that the annual deficit accruing to MMIA is almost $80 million (A. 1030). The actuaries' projections took into account the potential beneficial effects of the "tort reform" legislation (RA. 88, A. 1000).

The statutory scheme of future surcharges in no way "guarantees" that the current rate deficiencies will be recouped (*see* Respondent's Brief at 10, 12, 19). If physicians will leave the state or "go bare" when confronted with substantial premium increases—as the Superintendent has reported to the Governor and Legislature (*see* Petition at 9 n.11)—then, manifestly, there will be no future policyholders to pay the surcharges. Furthermore, the Superintendent failed to bring about a condition precedent to the scheme for recoupment of the deficits through future surcharges. Rates were not brought to adequate levels commencing July 1, 1988, as the Superintendent's actuary had testified would be necessary (Petition at 8 n.10). Although the court below recognized that the condition precedent was part of the actuary's recoupment assumptions, *MMIA v. Superintendent*, 72 N.Y.2d at 764 (Petition App. A at 10a-11a), it failed to recognize that the condition had not occurred.

The trial court appropriately found, based on the evidence adduced, that the statutory scheme for recoupment "depends upon future results which themselves rest on a speculative foundation with no basis in past experience." (Petition, App. D at 34a). The scheme certainly is not the type of "reasonable, certain and adequate" compensation which this Court has stated is necessary in taking cases. *See Williamson County Regional Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 194 (1985) (cited at Respondent's Brief at 11).

The Superintendent's attempt to dissuade this Court from reviewing the decision below based on the pendency of *Alliance*

of *American Insurers v. Cuomo*, 87 Civ. 0169 (Patterson, U.S.D.J.) also must fail. MMIA is not a party to the *Alliance* lawsuit. The issues of whether New York can compel MMIA to operate at a loss and whether MMIA has standing to assert a claim of confiscation are only before this Court, not the *Alliance* court. MMIA, through protracted proceedings below, has established that it is incurring huge deficits as a direct result of state-prescribed confiscatory rates. The New York Court of Appeals' holding that MMIA cannot assert a constitutional claim against this taking requires immediate review by this Court.

II.

Fifth and Fourteenth Amendment Protections Extend to Non-Profit Joint Underwriting Associations

Respondent's Brief seems to concede that MMIA would have a valid constitutional claim—so that the decision below would be clearly erroneous—if only MMIA had "investment-backed expectations" (Respondent's Brief at 7). However, no such criteria for fifth and fourteenth amendment protections are prescribed either by the Constitution or the decided cases. To the contrary, this Court in *California State Automobile Association Inter-Insurance Bureau v. Maloney*, 341 U.S. 105 (1951) recognized a due-process challenge by a state-mandated, non-profit automobile risk insurance pool. Confiscation was held not to be a factor only because the premiums chargeable were commensurate with the risks.

Similarly, lower federal courts have recognized due-process claims of non-profit entities. *See St. Francis Hosp. Center v. Heckler*, 714 F.2d 872, 875 (7th Cir. 1983) ("the government cannot prescribe rates so low that the result is a taking of property without just compensation") (citation omitted), *cert. denied*, 465 U.S. 1022 (1984); *Delaware River Port Auth. v. Tiemann*, 403 F. Supp. 1117, 1124-25 (D.N.J. 1975) (non-profit entity entitled to a reasonable and just rate, which enables it to maintain its operations), *vacated*, 531 F.2d 699 (3d Cir.), *reinstated on remand*, 421 F. Supp. 142 (D.N.J. 1976).

Both Respondent's Brief, at 4, and the decision below, *MMIA v. Superintendent*, 72 N.Y.2d at 766 (Petition, App. A at 13a) concede that the "funds and reserves of MMIA are held and invested separately from its members." Like any other state-chartered insurance company, MMIA sets aside funds collected from policyholders as reserves to meet obligations assumed under the policies.[4] The decision below would allow the State to take these funds—which already are woefully inadequate to meet outstanding policy obligations—without MMIA having any recourse under the fifth and fourteenth amendments.

As the states grapple with problems of uninsurable risks, the need for resolution of this issue becomes urgent. Should this Court decline to grant certiorari, other states likely will follow New York's lead in compelling state-created JUA's to provide insurance at inadequate rates for certain groups of persons within the states. Issuance of a writ of certiorari to the New York Court of Appeals will provide opportunity for this Court to define the permissible limits of state ratemaking authority so as to avoid the proliferation of unconstitutional rate schemes similar to that upheld by the decision below.

In *Duquesne Light Co. v. Barasch*, 109 S. Ct. 609 (1989), Chief Justice Rehnquist, writing for the majority, reiterated the principle that an unconstitutional result may be established where the total effect of the rate scheme is unreasonable. *Id.* at 617. It is the total effect of the rating scheme foisted upon MMIA that is challenged as unconstitutional. Whether a JUA can be compelled to operate at a loss for a period of at least fifteen years in the hope that the enormous deficits will be made up by speculative future surcharges is a question requiring review by this Court.

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4 MMIA's latest annual statement filed with the Superintendent shows assets of over $700 million and liabilities in excess of $1 billion. Medical Malpractice Insurance Association, 1988 Annual Statement 2-3 (1989).

CONCLUSION

For the foregoing reasons and those set forth in the Petition, it is respectfully submitted that the Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX

Opinion and Judgment of the Court of Appeals of the State of New York

COURT OF APPEALS
STATE OF NEW YORK

1 No. 88

MEDICAL MALPRACTICE INSURANCE ASSOCIATION,

Respondent,

—v.—

MARIO M. CUOMO, &c. et al.,

Appellants.

MEMORANDUM

This memorandum is uncorrected and subject to revision before publication in the New York Reports.

Robert Abrams, Attorney General (Kathie Ann Whipple, O. Peter Sherwood, Richard G. Liskov of counsel) for appellants.

T. Richard Kennedy, Larry P. Schiffer, Michael A. Knoerzer, Paul D. Getzels, Richard J. Cairns, NY City, for respondent.

MEMORANDUM:

The order of the Appellate Division should be reversed, with costs, the preliminary injunction vacated, defendant's motion for summary judgment granted, and section 11 and section 40 of chapter 266 of the laws of 1986 declared constitutional. The certified question should be answered in the negative.

We have recently determined that the Legislature may require the Medical Malpractice Insurance Association (MMIA) to operate at a loss on a temporary or even continual basis in order to promote affordable medical malpractice coverage (*Matter of Medical Malpractice Insurance Assn v Superintendent of Insurance*, 72 NY2d 753, 766). In so holding, we rejected the argument that § 40 of the Medical Malpractice Reform Act of 1986 (Reform Act) is confiscatory as to MMIA because it authorizes the Superintendent of Insurance to consider future surcharges on insurance premiums in fixing present insurance rates and thus contemplates that MMIA may be required to operate at a deficit. Likewise here, there is no constitutional infirmity in § 11 of the Reform Act insofar as it directs MMIA to refund stabilization reserve fund charges collected on excess policies issued during the 1985-1986 policy year. As a creature of statute, MMIA had no vested property interest in those charges and it was within the Legislature's prerogative to direct a refund in an effort to reduce overall health care costs (*see*, *Matter of Medical Malpractice Insurance Assn v Superintendent of Insurance*, 72 NY2d at 766, *supra*). Nor can MMIA state any cognizable claim for the impairment of contract rights since the stabilization reserve fund charge on excess insurance policies was imposed by statute and not as the result of any bargaining between MMIA and its insureds.

* * *

Order reversed, with costs, preliminary injunction vacated, defendants' motion for summary judgment granted and section 11 and section 40 of Chapter 266 of the Laws of 1986 declared constitutional in a memorandum. Certified question answered in the negative. Chief Judge Wachtler and Judges Simons, Kaye, Alexander, Titone, Hancock and Bellacosa concur.

Decided May 2, 1989

Remittitur

COURT OF APPEALS
STATE OF NEW YORK

The Hon. Sol Wachtler, Chief Judge, Presiding

1 No. 88

MEDICAL MALPRACTICE INSURANCE ASSOCIATION,

Respondent,

—v.—

MARIO M. CUOMO, &c. et al.,

Appellants.

The appellant(s) in the above entitled appeal appeared by HON. ROBERT ABRAMS, Attorney General of the State of New York; the respondent appeared by WERNER KENNEDY & FRENCH, ESQS.

The Court, after due deliberations, orders and adjudges that the order is reversed, with costs, preliminary injunction vacated, defendants' motion for summary judgment granted and section 11 and section 40 of Chapter 266 of the Laws of 1986 declared constitutional in a memorandum. Certified question answered in the negative. Chief Judge Wachtler and Judges Simons, Kaye, Alexander, Titone, Hancock and Bellacosa concur.

The Court further orders that the papers required to be filed and this record of the proceedings in this Court be remitted to the Supreme Court, New York County, there to be proceeded upon according to law.

I certify that the preceding contains a correct record of the proceedings in this appeal in the Court of Appeals and that the papers required to be filed are attached.

/s/ DONALD M. SHERAW

Donald M. Sheraw,
Clerk of the Court

Court of Appeals, Clerk's Office,
Albany, May 2, 1989